

To Our Shareholders:

Zayre Corp. achieved sharply higher earnings during the third fiscal quarter and record operating results for the year to date.

Volume during the 13 weeks ended October 28, 1978 (excluding sales of leased departments) rose 8.8% to \$340,459,000 and net income increased to \$4,363,000, or \$.84 per primary share, up from \$3,143,000 or \$.62 per share last year.

For the nine month period to date, total sales (excluding those of leased departments) rose 10.1% to \$936,285,000 and net income totaled \$6,060,000, or \$1.16 per primary share, as compared with \$4,422,000, or \$.86 per share in 1977.

Net earnings for the full 52 week trailing year period through October 28 aggregated \$13,394,000, or \$2.63 per primary share, versus \$11,261,000 or \$2.23 per share in the comparable prior period.

Sales gains in our Zayre stores have continued to be quite positive, although at a somewhat more moderate rate than in the first half. Apparel volume has been particularly outstanding, which is most helpful to overall merchandise margins.

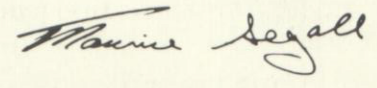
Thirty-six "Hit or Miss" off-price, women's fashion apparel shops have been added during the nine month period and 212 are expected to be in operation by year end. "T. J. Maxx", our new

off-price, brand name, family "apparel super-market", has developed well and, in its second year, will shortly have 19 units in operation.

Good results have been achieved in our efforts to contain the growth of inventories to that of our sales. Short term seasonal borrowings in support of our peak requirements are higher than a year ago but will be entirely cleared in December, well before the end of our fiscal year, as is our consistent practice.

Our stores, merchandise assortments, and promotional programs are well set for the upcoming holiday season. While we will be comparing against a strong 1977 fourth quarter, we are encouraged by the Company's progress and current performance and anticipate a successful year.

Respectfully submitted,

SUMNER FELDBERG
Chairman of the Board

MAURICE SEGALL
President

November 15, 1978

Zayre Corp. and Consolidated Subsidiaries

CONDENSED BALANCE SHEETS *(Unaudited)*

(Dollars in Millions)

	October 28, 1978	October 29, 1977
ASSETS		
Current assets		
Cash	\$ 14.2	\$ 19.0
Accounts receivable and prepaid expenses	23.5	20.4
Merchandise inventories	392.2	350.5
Total current assets	429.9	389.9
Property, net of depreciation and amortization	86.8	82.6
Other assets	9.4	9.3
TOTAL ASSETS	\$526.1	\$481.8
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Notes payable to banks	\$ 62.0	\$ 40.0
Current instalments of long-term debt ...	8.6	10.7
Accounts payable and accrued expenses .	205.0	190.2
Total current liabilities	275.6	240.9
Long-term debt (includes real estate mortgages)	96.3	100.8
Deferred income taxes	10.6	10.1
Shareholders' equity	143.6	130.0
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	\$526.1	\$481.8

FINANCIAL SUMMARY *(Unaudited)*

(Dollars in Thousands Except Per Share Amounts)

	13 Weeks October 28, 1978
Net sales (excluding leased department sales)	\$340,459
Income before income taxes	8,390
Provision for federal and state income taxes	4,027
Net income	\$ 4,363
Net income per common share:	
Primary	\$.84
Fully diluted	\$.79
Average number of common shares outstanding for primary computation	5,161,309
Self-service department stores in operation	253

(1) The Company's fiscal year ends on the last Saturday in January.

<i>Ended</i>	<i>39 Weeks Ended</i>		<i>52 Weeks Ended⁽¹⁾</i>	
<i>October 29, 1977</i>	<i>October 28, 1978</i>	<i>October 29, 1977</i>	<i>October 28, 1978</i>	<i>October 29, 1977</i>
\$312,910	\$936,285	\$850,098	\$1,347,488	\$1,216,303
6,557	11,654	9,222	25,849	23,725
3,414	5,594	4,800	12,455	12,464
\$ 3,143	\$ 6,060	\$ 4,422	\$ 13,394	\$ 11,261
\$.62	\$1.16	\$.86	\$2.63	\$2.23
\$.59	\$1.14	\$.86	\$2.48	\$2.13
983,750	5,106,708	4,983,698	5,084,976	4,976,396

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CONDENSED STATEMENTS OF CHANGES IN FINANCIAL POSITION (*Unaudited*)

(Dollars in Millions)

	<i>39 Weeks Ended</i>	
	<i>October 28, 1978</i>	<i>October 29, 1977</i>
SOURCE OF WORKING CAPITAL		
Funds provided from operations	\$ 15.8	\$ 14.2
Additional long-term borrowings	5.2	3.5
Property disposals at net book value4	3.4
Other3	—
	<u>\$ 21.7</u>	<u>\$ 21.1</u>
APPLICATION OF WORKING CAPITAL		
Decrease in long-term debt	6.1	7.6
Purchase of sinking fund debentures	1.5	1.1
Property additions	13.1	7.0
Other6	1.5
	<u>21.3</u>	<u>17.2</u>
Increase in working capital4	3.9
	<u>\$ 21.7</u>	<u>\$ 21.1</u>
DETAILS OF WORKING CAPITAL INCREASE		
Increase (decrease) in current assets:		
Cash	(9.4)	(6.8)
Marketable securities	(12.0)	(12.0)
Accounts receivable and prepaid expenses	12.9	11.1
Merchandise inventories	149.9	139.4
	<u>141.4</u>	<u>131.7</u>
Increase (decrease) in current liabilities:		
Notes payable	62.0	40.0
Current instalments of long-term debt ...	(1.4)	(.6)
Accounts payable and accrued expenses .	80.4	88.4
	<u>141.0</u>	<u>127.8</u>
Increase in working capital	<u>\$.4</u>	<u>\$ 3.9</u>

Zayre

Third Quarter Report to Shareholders

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